

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2014

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from – to –

Commission file number: 001-35629

TILE SHOP HOLDINGS, INC.
(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation)

45-5538095
(I.R.S. Employer
Identification No.)

14000 Carlson Parkway
Plymouth, Minnesota
(Address of principal executive offices)

55441
(Zip Code)

(763) 852-2901
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

As of May 5, 2014, there were 51,241,127 shares of the registrant's common stock, par value \$0.0001 per share, outstanding.

TILE SHOP HOLDINGS, INC.
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Tile Shop Holdings, Inc. and Subsidiaries
Condensed Consolidated Balance Sheets
(in thousands, except share amounts)

	March 31, 2014 (unaudited)	December 31, 2013 (audited)
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 4,287	\$ 1,761
Trade receivables, net	1,506	1,198
Inventories	66,282	72,067
Income tax receivable	4,013	9,528
Deferred tax and other current assets, net	6,148	7,150
Total Current Assets	82,236	91,704
Property, plant and equipment, net	132,449	125,317
Deferred taxes and other assets	25,498	25,748
TOTAL ASSETS	\$ 240,183	\$ 242,769
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 13,517	\$ 22,867
Other accrued liabilities	19,441	17,118
Total Current Liabilities	32,958	39,985
Long-term debt, net	89,750	91,646
Capital lease obligation, net	1,078	1,161
Deferred rent	27,151	25,560
Other long-term liabilities	4,272	4,554
TOTAL LIABILITIES	155,209	162,906
Stockholders' equity:		
Common stock, par value \$.0001; authorized: 100,000,000 shares; issued: 51,241,127, and 51,229,720 shares	5	5
Preferred stock, par value \$.0001; authorized: 10,000,000 shares; issued: 0 shares	-	-
Additional paid-in-capital	171,121	169,719
Retained (deficit) earnings	(86,152)	(89,861)
Total stockholders' equity	84,974	79,863
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 240,183	\$ 242,769

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

Tile Shop Holdings, Inc. and Subsidiaries
Condensed Consolidated Statements of Income
(in thousands, except share and per share amounts) (unaudited)

	Three months ended March 31,	
	2014	2013
Net sales	\$ 64,379	\$ 56,835
Cost of sales	19,446	16,462
Gross profit	44,933	40,373
Selling, general and administrative expenses	37,972	28,354
Income from operations	6,961	12,019
Interest expense	711	594
Change in fair value of warrants	0	51,845
Other expense	69	33
Income (loss) before income taxes	6,181	(40,453)
Provision for income taxes	(2,472)	(4,264)
Net income (loss)	<u>\$ 3,709</u>	<u>\$ (44,717)</u>
Earnings (loss) per common share:		
Basic	\$ 0.07	\$ (1.00)
Diluted	\$ 0.07	\$ (1.00)
Weighted average shares outstanding:		
Basic	51,166,766	44,854,988
Diluted	51,523,170	44,854,988

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

Tile Shop Holdings, Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows
(in thousands)
(unaudited)

	Three months ended March 31,	
	2014	2013
Cash Flows From Operating Activities		
Net income (loss)	\$ 3,709	\$ (44,717)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	4,459	3,074
Loss on disposals of property, plant and equipment	91	45
Change in fair value of warrants	-	51,845
Deferred rent	1,591	1,831
Stock based compensation	1,397	1,092
Deferred income taxes	-	(281)
Changes in operating assets and liabilities:		
Trade receivables	(308)	(273)
Inventories	5,785	(2,190)
Deferred taxes and other assets	(8)	(568)
Accounts payable	(9,350)	446
Income tax receivable/ payable	5,515	4,211
Accrued expenses and other liabilities	2,326	3,745
Net cash provided by operating activities	<u>15,207</u>	<u>18,260</u>
Cash Flows From Investing Activities		
Proceeds from cash surrender value of life insurance policy	462	-
Purchases of property, plant and equipment	(12,073)	(11,143)
Proceeds from the sale of property, plant and equipment	159	-
Net cash used in investing activities	<u>(11,452)</u>	<u>(11,143)</u>
Cash Flows From Financing Activities		
Release of restricted cash	754	-
Payments of long-term debt and capital lease obligations	(958)	(6,058)
Net payments on line of credit	(1,026)	-
Repurchase of warrants	-	(30,108)
Proceeds from exercise of warrants	-	41,821
Proceeds from exercise of stock options	5	-
Security deposit	(4)	4
Net cash (used in) provided by financing activities	<u>(1,229)</u>	<u>5,659</u>
Net change in cash	2,526	12,776
Cash and cash equivalents beginning of period	1,761	2,987
Cash and cash equivalents end of period	<u>\$ 4,287</u>	<u>\$ 15,763</u>
Non cash items		
Reclassification of warrants from liability to equity	\$ -	\$ 110,002
Increase in other assets for exercise of warrants	\$ -	\$ 3,332
Purchases of property, plant and equipment included in accounts payable and accrued expenses	\$ -	\$ 1,455

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

Tile Shop Holdings, Inc. and Subsidiaries
Notes to Consolidated Financial Statements
(unaudited)

Note 1: Organization and Nature of Business

The Tile Shop, LLC (“The Tile Shop”) was formed on December 30, 2002, as a Delaware limited liability company (LLC) and began operations on January 1, 2003. Tile Shop Holdings, Inc. (“Holdings”, and, together with its wholly owned subsidiaries, the “Company”) was incorporated under the laws of the state of Delaware in August 2012 to become the parent Company of Tile Shop, LLC.

The Company is engaged in the sale of tile and flooring products. The Company also fabricates or manufactures setting and maintenance materials in Michigan, Wisconsin, Virginia and Oklahoma. The Company’s primary market is retail sales to consumers; however, the Company does have sales to contractors. As of March 31, 2014, the Company had 93 stores in 30 states and an on-line retail operation. The Company also has distribution centers located in Wisconsin, Michigan, Virginia and Oklahoma.

The consolidated financial statements of the Company include the accounts of its wholly owned subsidiaries, and variable interest entities. All significant intercompany transactions have been eliminated in consolidation.

Note 2: Unaudited Consolidated Financial Statements

The information furnished in this report is unaudited and reflects all adjustments which are normal recurring adjustments that, in the opinion of management, are necessary to fairly present the operating results for the interim periods. The operating results for the interim periods presented are not necessarily indicative of the operating results to be expected for the full fiscal year. The unaudited interim condensed consolidated financial statements for the three months ended March 31, 2014, should be read in conjunction with the audited consolidated financial statements and footnotes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2013, previously filed with the Securities and Exchange Commission on February 28, 2014.

Note 3: Summary of Selected Significant Accounting Policies

A detailed description of our significant accounting policies can be found in our most recent Annual Report filed on Form 10-K for the year ended December 31, 2013. There were no material changes in significant accounting policies during the quarter ended March 31, 2014.

Inventories:

Inventories are stated at the lower of cost (determined on the first-in, first-out method) or market. Inventories consist primarily of merchandise held for sale. Inventories were comprised of the following as of March 31, 2014 and December 31, 2013:

	(in thousands)	
	March 31, 2014	December 31, 2013
Finished goods	\$ 59,874	\$ 62,690
Raw materials	1,933	1,370
Finished goods in transit and prepaid inventory	4,475	8,007
Total	<u>\$ 66,282</u>	<u>\$ 72,067</u>

Income Taxes:

The Company’s effective tax rate on net income before income taxes for the three month periods ended March 31, 2014 and 2013 was 40% and (10.5)% respectively. The effective tax rate on net loss before income taxes for the three month period ending March 31, 2013 was due to the significant non-deductible expense for the change in warrant liability. For the three month periods ended March 31, 2014 and 2013, the Company recorded an income tax provision of \$2,472 and \$4,264, respectively.

The Company recognizes deferred tax liabilities and assets for the expected future tax consequences of events that have been included in the financial statements or tax returns. Deferred tax liabilities and assets are determined based on the difference between the financial statement basis and tax basis of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. The Company estimates the degree to which tax assets and credit carryforwards will result in a benefit based on expected profitability by tax jurisdiction. A valuation allowance for such tax assets and loss carryforwards is provided when it is determined to be more likely than not that the benefit of such deferred tax asset will not be realized in future periods. If it becomes more likely than not that a tax asset will be used, the related valuation allowance on such assets would be reduced.

Tile Shop Holdings, Inc. and Subsidiaries
Notes to Consolidated Financial Statements
(unaudited)

Earnings Per Share:

Basic earnings per share is calculated by dividing net income (loss) by the weighted-average number of shares outstanding during the period. Diluted earnings (loss) per share is calculated by dividing net income (loss) by the weighted-average number of common shares outstanding, after giving effect to all dilutive potential common shares outstanding during the period. For the three months ended March 31, 2013, diluted net loss per share is identical to basic net loss per share as all potentially dilutive securities have been excluded from the calculation of diluted net loss per common share because the inclusion of such securities would be anti-dilutive.

Basic and diluted earnings (loss) per share were calculated as follows:

	(in thousands, except share and per share data)	
	For the three months ended March 31,	
	2014	2013
Net income (loss)	\$ 3,709	\$ (44,717)
Weighted-average shares outstanding – basic	51,166,766	44,854,988
Effect of diluted securities attributable to stock-based payments	356,404	-
Weighted-average shares outstanding – diluted	51,523,170	44,854,988
Earnings per share from continuing operations:		
Basic	\$ 0.07	\$ (1.00)
Diluted	\$ 0.07	\$ (1.00)

Potentially dilutive securities include 2,404,417 options and 259,394 restricted shares outstanding as of March 31, 2014.

Note 4: Other Accrued Liabilities

Other accrued liabilities consisted of the following at:

	(in thousands)	
	March 31, 2014	December 31, 2013
Customer deposits	\$ 6,694	\$ 5,301
Accrued wages and salaries	3,034	2,905
Taxes - other	2,424	1,783
Interest payable	310	409
Sales return reserve	3,100	2,850
Current portion of debt and capital lease obligation	3,879	3,870
	<u>\$ 19,441</u>	<u>\$ 17,118</u>

Note 5: Long-term Debt

On October 3, 2012, the Company and its operating subsidiary The Tile Shop, LLC entered into a credit agreement with Bank of America, N.A. (the “Credit Agreement”). The Credit Agreement, as amended, provides the Company with a \$120 million senior secured credit facility, comprised of a five-year \$25 million term loan and a \$95 million revolving line of credit. The Amended Credit Agreement is secured by virtually all of the assets of the Company, including but not limited to, inventory, receivables, equipment and real property. Borrowings pursuant to the Credit Agreement bear interest at either a base rate or a LIBOR-based rate, at the option of the Company. The LIBOR-based rate will range from LIBOR plus 1.75% to 2.25%, depending on The Tile Shop’s leverage ratio. The base rate is equal to the greatest of: (a) the Federal funds rate plus 0.50%, (b) the Bank of America “prime rate,” and (c) the Eurodollar rate plus 1.00%, in each case plus 0.75% to 1.25% depending on The Tile Shop’s leverage ratio. At March 31, 2014 and December 31, 2013, the base interest rate was 4.25%. At March 31, 2014 and December 31, 2013 the Libor-based interest rate was 2.156% and 2.408% respectively. As of March 31, 2014 and December 31, 2013, the Company had outstanding borrowings related to the revolving line of credit of \$72.5 million and \$73.5 million, respectively. The term loan requires quarterly principal payments of \$0.9 million. The Credit Agreement contains customary events of default, conditions to borrowings, and restrictive covenants, including restrictions on the Company’s and The Tile Shop’s ability to dispose of assets, make acquisitions, incur additional debt, incur liens, make investments, or enter into transactions with affiliates on other than on terms that could be obtained in an arm’s length transaction. The Credit Agreement also includes financial and other covenants including covenants to maintain certain fixed charge coverage ratios and rent adjusted leverage ratios. In addition, except with respect to pro rata payments made by The Tile Shop or other subsidiaries to the Company or any other equity owner of such entity, the Credit Agreement prohibits the payments of cash dividends. The Company was in compliance with the covenants as of March 31, 2014. On March 26, 2014, the Company completed an amendment to the Credit Facility which modified certain financial covenants to reflect the ongoing growth of the business.

Tile Shop Holdings, Inc. and Subsidiaries
Notes to Consolidated Financial Statements
(unaudited)

Note 6: Fair Value of Financial Instruments

These condensed consolidated financial statements include the following financial instruments: cash and cash equivalents, trade receivables, accounts payable, accrued expenses, capital leases, notes payable and debt. At March 31, 2014 and December 31, 2013, the carrying amount of the Company's cash and cash equivalents and trade receivables, accounts payable and accrued expenses approximated their fair values due to their short maturities. The carrying value of the Company's borrowings and capital lease obligation approximates fair value based upon the market interest rates available to the Company for debt and capital lease obligations with similar risk and maturities.

Fair value is the price that would be received to sell an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. To measure fair value, the Company uses a three-tier valuation hierarchy based upon observable and non-observable inputs:

Level 1 – Unadjusted quoted prices that are available in active markets for the identical assets or liabilities at the measurement date.

Level 2 – Significant other observable inputs available at the measurement date, other than quoted prices included in Level 1, either directly or indirectly, including:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets in non-active markets;
- Inputs other than quoted prices that are observable for the asset or liability; and
- Inputs that are derived principally from or corroborated by other observable market data.

Level 3 – Significant unobservable inputs that cannot be corroborated by observable market data and reflect the use of significant management judgment. These values are generally determined using pricing models for which the assumptions utilize management's estimates of market participant assumptions.

Note 7: Equity Incentive Plans

Stock based compensation:

The Company measures and recognizes compensation expense for all stock-based awards at fair value. The financial statements for the three months ended March 31, 2014 and 2013 include compensation cost for the portion of outstanding stock option awards which have vested during those periods. The Company recognizes stock option compensation costs on a straight-line basis over the requisite service period of the award, which is generally the option vesting term. For the three months ended March 31, 2014 and 2013 total stock option compensation was \$1.0 million and \$0.8 million, respectively, and was included in selling, general and administrative expenses in the accompanying condensed consolidated statements of income.

As of March 31, 2014, the Company had 2,487,000 outstanding stock-based awards at a weighted average exercise price of \$13.88.

Restricted stock:

The Company awards restricted common shares to selected employees, and non-employee directors. Recipients are not required to provide any consideration other than continued service. Company share awards are subject to certain restrictions on transfer, and all or part of the shares awarded may be subject to forfeiture upon the occurrence of certain events, including employment termination. The restricted stock is valued at its grant date fair value and expensed over the requisite service period or the vesting term of the awards. For the three months ended March 31, 2014 and 2013 total stock based compensation was \$0.4 million and \$0.3 million, respectively, was included in selling, general and administrative expenses in the accompanying condensed consolidated statements of income.

Note 8: Warrants

During 2012, the Company evaluated warrants under Accounting Standards Codification ("ASC") Subtopic 815-40, Contracts in Entity's Own Equity. ASC Section 815-40-15 addresses equity versus liability treatment and classification of equity-linked financial instruments, including common stock purchase warrants, and states that a warrant may be classified as a component of equity only if, among other things, the warrant is indexed only to the issuer's common stock. Under ASC Section 815-40-15, a warrant is not indexed to the issuer's common stock if the terms of the warrant require an adjustment to the exercise price upon a specified event and that event is not an input to the fair value of the warrant. Based on its evaluation, the Company concluded that our warrants were not indexed to the Company's common stock in the manner contemplated by ASC Section 815-40-15 because the transactions that will trigger the Price Reduction Provision are not inputs to the fair value of the warrants. Accordingly, the existence of the Price Reduction Provision in the warrants required us to classify the warrants as a derivative liability.

As of March 31, 2014 and December 31, 2013, the Company had no outstanding warrants and no liability. As of March 31, 2013, the change in fair value of warrants was \$51.8 million.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2013 and our consolidated financial statements and related notes appearing elsewhere in this Quarterly Report on Form 10-Q.

Forward-Looking Statements

This Quarterly Report on Form 10-Q contains "forward-looking statements" that involve risks and uncertainties, as well as assumptions that, if they never materialize or prove incorrect, could cause our results to differ materially from those expressed or implied by such forward-looking statements. The statements contained in this Quarterly Report on Form 10-Q that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, or Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, or Exchange Act. Forward-looking statements are often identified by the use of words such as, but not limited to, "anticipate," "believe," "can," "continue," "could," "estimate," "expect," "intend," "may," "will," "plan," "project," "seek," "should," "target," "will," "would," and similar expressions or variations intended to identify forward-looking statements. These statements are based on the beliefs and assumptions of our management based on information currently available to management. Such forward-looking statements are subject to risks, uncertainties and other important factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, unexpected delays or expenses related to opening new stores and maintaining existing stores, uncertain impact of our expansion strategy on existing store sales and our financial condition, changes to economic conditions and customer preferences, disruptions in our supply chain, competitive factors, increases to interest rates, inability to maintain or procure credit, unanticipated expenses related to operating as a public company, an inability to maintain effective internal control over financial reporting, and those factors disclosed in the section captioned "Risk Factors" in our Annual Report for the fiscal year ended December 31, 2013, filed with the Securities and Exchange Commission. Furthermore, such forward-looking statements speak only as of the date of this report. Except as required by law, we undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements.

Business Combination Transaction

We were incorporated in the State of Delaware in June 2012. On August 21, 2012, we consummated a business combination (the "Business Combination") with JWC Acquisition Corp. ("JWCAC") in order to become the parent company of The Tile Shop, LLC ("The Tile Shop") and, in connection therewith, became a successor issuer to JWCAC by operation of Rule 12g-3(a) promulgated under the Securities Exchange Act of 1934, as amended (the "Exchange Act").

Overview and Recent Developments

We are a specialty retailer of manufactured and natural stone tiles, setting and maintenance materials, and related accessories in the United States. We offer a wide selection of products, attractive prices, and exceptional customer service in an extensive showroom setting. As of March 31, 2014 we operated 93 stores in 30 states, with an average size of 23,000 square feet. We also sell our products on our website.

We purchase our tile products and accessories directly from producers and manufacture our own setting and maintenance materials, such as thinset, grout, and sealers. We believe that our long-term producer relationships, together with our design, manufacturing and distribution capabilities, enable us to offer a broad assortment of high-quality products to our customers, who are primarily homeowners, at competitive prices. We have invested significant resources to develop our proprietary brands and product sources and believe that we are a leading retailer of stone tiles, accessories, and related materials in the United States.

Our focus in 2014 is to expand our brand by opening twenty new stores in 2014 and to improve the performance of our existing stores. During the three months ended March 31, 2014, we opened five stores in Illinois and Arizona, New Mexico and Texas, further expanding our footprint in the southwest. We believe that the highly-fragmented U.S. retail tile market provides us with a significant opportunity to expand our store base in the United States and Canada. We expect store base growth will drive productivity and operational efficiencies. Our growth plans also require us to maintain significant inventory on-hand in order to fulfill orders and prevent delay at these new locations.

For the three months ended March 31, 2014 and 2013, we reported net sales of \$64.4 million and \$56.8 million, respectively, and income from operations of \$7.0 million and \$12.0 million, respectively. From December 31, 2009 to December 31, 2013, our net sales and income from operations increased at compounded annual growth rates of 18.5% and 7.9% respectively. During that period, we opened 47 new retail locations. We plan to continue to focus on store growth.

Net cash flows provided by operating activities were \$15.2 million and \$18.3 million for the three months ended March 31, 2014 and 2013, respectively, which were used to fund capital expenditures for opening new stores, pay down debt and daily operations. We expect to continue to fund our capital expenditures and daily operations from our operating cash flows and with borrowings pursuant to our credit facility. As of March 31, 2014, we had cash of \$4.3 million and working capital of \$49.3 million.

Key Components of our Consolidated Statements of Income

Net sales Net sales represents total charges to customers, net of estimated returns, and includes freight charged to customers. We recognize sales at the time that the customer takes possession of the merchandise or the merchandise has shipped. We recognize service revenue, which consists primarily of freight charges for home delivery, when the service has been rendered. We are required to charge and collect sales and other taxes on sales to our customers and remit these taxes back to government authorities. Sales and other taxes are recorded in the consolidated balance sheets but excluded from the consolidated statements of income. The increase in net sales in recent years has been a result of store base growth, increases in same store sales, expansion of product lines, and a gradually improving national economy.

The table below sets forth information about our same store sales growth from the year ended December 31, 2011 through March 31, 2014. The growth since 2011 through 2013 was driven by incremental net sales from stores not included in the comparable stores base, and the modest decrease in the same store sales during the period ending March 31, 2014 was the result of harsh winter weather conditions in important mid-west, mid-Atlantic and east coast markets where the majority of our stores are located. Same store sale amounts include total charges to customers less any actual returns. We do not include estimated return provisions or sales allowances in the same store sales calculation, as return reserves are calculated at the consolidated level. In general, we consider a store comparable on the first day of the 13th month of operation.

	Three Months Ended March 31,		Years Ended December 31,		
	2014	2013	2013	2012	2011
Same store sales growth (decline)	(2.3%)	10.4%	12.4%	7.1%	6.4%

We opened twenty, fifteen and five new stores in 2013, 2012 and 2011, respectively, as well as five new stores in the three months ended March 31, 2014. Net sales at new stores are generally lowest in the first few months after a location is opened and generally increase over time. We expect a store's net sales to increase faster during its first three years of operation than in its later years. Store locations opened in existing markets tend to have higher net sales in the first year of operation than store locations opened in new markets because of increased brand awareness in existing markets and because a portion of such net sales come from more mature stores in those markets.

Cost of sales Cost of sales consists primarily of material costs, freight, duties, and storage and delivery of product to customers from stores, as well as costs associated with manufacturing of maintenance materials.

Gross profit Gross profit is net sales less cost of sales. Gross margin is the percentage determined by dividing gross profit by net sales.

Selling, general, and administrative expenses Payroll costs and occupancy expenses have historically been our most significant selling, general, and administrative expenses. Payroll costs exclude costs associated with manufacturing labor, as those costs are included in cost of sales. For the three months ended March 31, 2014 and 2013, our selling, general, and administrative expenses as a percentage of net sales was 59.0% and 49.9%, respectively. Our payroll costs have increased as a percentage of net sales primarily due to increased store base growth and investments in support infrastructure. Our occupancy costs have increased as a percentage of net sales due to opening 20 new stores in 2013 and 5 new stores in the three months ended March 31, 2014. Since new store sales are lower in the first months after opening, we anticipate that our selling, general and administrative expenses as a percentage of net sales will increase as we add store related occupancy and sales personnel costs. We will also add corporate leadership and staff costs and other corporate infrastructure investments to support our growth.

Pre-opening costs Our pre-opening costs are those typically associated with the openings of a new store and generally include rent expense, payroll costs, occupancy costs and promotional costs. Pre-opening costs are expensed as incurred and recorded in selling, general and administrative expenses.

Income taxes We are subject to income tax in the United States as well as other tax jurisdictions in which we conduct business. Our effective tax rate for the three months ended March 31, 2014 is not necessarily indicative of the effective tax rate that may be expected for future periods.

Adjusted EBITDA

We calculate Adjusted EBITDA by taking net income calculated in accordance with GAAP, and adjusting interest expense, income taxes, depreciation and amortization, non-cash change in fair value of warrants, stock based compensation and other non-recurring items including special investigation costs and equity related transaction costs. Adjusted EBITDA margin is equal to Adjusted EBITDA divided by net sales. We believe that these non-GAAP measures of financial results provide useful information to management and investors regarding certain financial and business trends relating to our financial condition and results of operations. Our management uses these non-GAAP measures to compare our performance to that of prior periods for trend analyses, for purposes of determining management incentive compensation, and for budgeting and planning purposes. These measures are used in financial reports prepared for management and our board of directors. We believe that the use of these non-GAAP financial measures provides an additional tool for investors to use in evaluating ongoing operating results and trends and in comparing our financial measures with other specialty retailers, many of which present similar non-GAAP financial measures to investors.

Our management does not consider these non-GAAP measures in isolation or as an alternative to financial measures determined in accordance with GAAP. The principal limitation of these non-GAAP financial measures is that they exclude significant expenses and income that are required by GAAP to be recorded in our consolidated financial statements. In addition, they are subject to inherent limitations as they reflect the exercise of judgments by management about which expenses and income are excluded or included in determining these non-GAAP financial measures. In order to compensate for these limitations, management presents non-GAAP financial measures in connection with GAAP results. We urge investors to review the reconciliation of our non-GAAP financial measures to the comparable GAAP financial measures and not to rely on any single financial measure to evaluate our business.

The reconciliation of adjusted EBITDA to net (loss) income for the three months ended March 31, 2014 and 2013 is as follows:

	For the three months ended March 31	
	2014	2013
Net income (loss)	\$ 3,709	\$ (44,717)
Interest expense	711	594
Income taxes	2,472	4,264
Change in fair value of warrants	-	51,845
Depreciation and amortization	4,411	3,044
Non-recurring investigation related and other recurring costs	1,128	240
Stock-based compensation	1,397	1,092
Adjusted EBTIDA	<u>\$ 13,828</u>	<u>\$ 16,362</u>

Comparison of the Three Months Ended March 31, 2014 to the Three Months Ended March 31, 2013

	(in thousands)			
	2014	% of sales	2013	% of sales
Net sales	\$ 64,379		\$ 56,835	
Cost of sales	19,446	30.2%	16,462	29.0%
Gross profit	44,933	69.8%	40,373	71.0%
Selling, general and administrative expenses	37,972	59.0%	28,354	49.9%
Income from operations	6,961	10.8%	12,019	21.1%
Interest expense	711	1.1%	594	1.0%
Change in fair value of warrants	0	0.0%	(51,845)	(91.2%)
Other expense	69	(0.1%)	33	(0.1%)
Income before income taxes	6,181	9.6%	(40,453)	(71.2%)
Provision for income taxes	(2,472)	(3.8%)	(4,264)	(7.5%)
Net income (loss)	<u>\$ 3,709</u>	<u>5.8%</u>	<u>\$ (44,717)</u>	<u>(78.7%)</u>

Net sales Net sales increased by \$7.5 million, or 13.3%, for the three months ended March 31, 2014 compared to the three months ended March 31, 2013. This increase is primarily due to net sales of \$8.8 million from 21 new stores, partly offset by a modest decrease in comparable store sales of 2.3%, or \$1.3 million. Sales were impacted by harsh weather conditions in important mid-west, Mid Atlantic, and east coast markets where the majority of our stores are located.

Gross profit Gross profit increased \$4.6 million, or 11.3%, for the three months ended March 31, 2014 compared to the three months ended March 31, 2013, primarily due to the increase in net sales. Gross margin decreased from 71.0% for the three months ended March 31, 2013 to 69.8% for the three months ended March 31, 2014. The change was primarily driven by slightly higher product related costs and transportation expenses and product discounts.

Selling, general, and administrative expenses Selling, general, and administrative expenses increased \$9.6 million, or 33.9%, for the three months ended March 31, 2014 compared to the three months ended March 31, 2013. Selling, general, and administrative expenses as a percentage of net sales increased to 59.0% for the three months ended March 31, 2014 from 49.9% for the three months ended March 31, 2013. The increase in selling, general, and administrative expenses was primarily due to increased rent and occupancy costs of \$2.1 million, increased salaries and payroll costs of \$3.5 million and increased depreciation and amortization of \$1.4 million, as a result of opening new stores. Selling, general and administrative expense also included an increase of \$0.9 million in professional fees primarily relating to Audit Committee special investigation costs.

Income from operations and operating margin As a result of the above, income from operations decreased by \$5.1 million, or (42.1)%, for the three months ended March 31, 2014 compared to the three months ended March 31, 2013. Operating income margin decreased from 21.1% to 10.8% for the three months ended March 31, 2014 compared to the three months ended March 31, 2013. The decrease is due to the changes noted above in gross profit and selling, general and administrative expenses.

Pre-opening Costs Our pre-opening costs are those typically associated with the openings of a new store and generally include rent expense, payroll costs and promotional costs. We expense pre-opening costs as incurred and include these costs in selling, general and administrative expenses. During the three months ended March 31, 2014 and 2013, we reported pre-opening costs of \$0.6 million and \$0.3 million, respectively.

Interest expense Interest expense increased \$0.1 million, or 20.0%, for the three months ended March 31, 2014 compared to the three months ended March 31, 2013. The increase is due to additional borrowings under our credit facility.

Change in Fair Value of Warrants The decrease in change in fair value of warrant liability of \$51.8 million, relates to a non-cash charge for the change in the fair value of the outstanding warrants for the three months ended March 31, 2013. The warrants were assumed by the Company in connection with the Business Combination on August 21, 2012. Prior to March 31, 2014, the warrants were fully exercised or redeemed, and no further expense will be recorded for these warrants in future periods.

Income before income taxes We recorded net income before taxes of \$6.2 million for the three months ended March 31, 2014 compared to a net loss of \$40.5 million for the same period in the previous year. The loss during the three months ended March 31, 2013 was primarily as a result of the change in the fair value of the warrant liability. Excluding the change in fair value of warrants, which was \$51.8 million for the three months ended March 31, 2013, net income before taxes was \$11.4 million.

Provision for income taxes Income tax provision decreased \$1.8 million for the three months ended March 31, 2014 compared to the three months ended March 31, 2013 due to lower taxable income.

Liquidity and Capital Resources

Our principal liquidity requirements have been for working capital and capital expenditures. Our principal sources of liquidity are \$4.3 million of cash and cash equivalents at March 31, 2014, our cash flow from operations, and borrowings available under our credit facility. We expect to use this liquidity for general corporate purposes, including opening new stores, purchasing additional merchandise inventory and maintaining our existing stores.

On October 3, 2012, the Company and its operating subsidiary, The Tile Shop, LLC, entered into a credit facility with Bank of America, N.A. (the "Credit Agreement"). The Credit Agreement, as amended, provides the Company with a \$120 million senior secured credit facility, comprised of a five-year \$25 million term loan and a \$95 million revolving line of credit. The Credit Agreement is secured by virtually all of the assets of the Company, including but not limited to, inventory, receivables, equipment and real property. Borrowings pursuant to the Credit Agreement bear interest at either a base rate or a LIBOR-based rate, at the option of the Company. The LIBOR-based rate will range from LIBOR plus 1.75% to 2.25%, depending on The Tile Shop's leverage ratio. The base rate is equal to the greatest of: (a) the Federal funds rate plus 0.50%, (b) the Bank of America "prime rate," and (c) the Eurodollar rate plus 1.00%, in each case plus 0.75% to 1.25% depending on The Tile Shop's leverage ratio. At March 31, 2014 and December 31, 2013, the base interest rate was 4.25%. At March 31, 2014 and December 31, 2013 the LIBOR-based interest rate was 2.156% and 2.408%, respectively. As of March 31, 2014 and December 31, 2013, the Company had outstanding borrowings related to the revolving line of credit of \$72.5 million and \$73.5 million, respectively. The term loan requires quarterly principal payments of \$0.9 million. The Credit Agreement contains customary events of default, conditions to borrowings, and restrictive covenants, including restrictions on the Company's and The Tile Shop's ability to dispose of assets, make acquisitions, incur additional debt, incur liens, make investments, or enter into transactions with affiliates on other than on terms that could be obtained in an arm's length transaction. The Credit Agreement also includes financial and other covenants including covenants to maintain certain fixed charge coverage ratios and rent adjusted leverage ratios. In addition, except with respect to pro rata payments made by The Tile Shop or other subsidiaries to the Company or any other equity owner of such entity, the Credit Agreement prohibits the payment of cash dividends. The Company was in compliance with the covenants as of March 31, 2014. On March 26, 2014, the Company completed an amendment to the Credit Facility which modified certain financial covenants to reflect the ongoing growth of the business.

We believe that our cash flow from operations, together with our existing cash and cash equivalents, and borrowings available under our credit facility will be sufficient to fund our operations and anticipated capital expenditures over at least the next 12 months.

Capital expenditures in the quarter were \$12.1 million. Approximately \$9.5 million of this was for new store build-out and remodels of existing stores, \$1.4 million was for expansion of our distribution and manufacturing facilities, and the remainder was for general corporate purposes, including expanding our existing information technology infrastructure.

Our future capital requirements will vary based on the number of additional stores, distribution centers, and manufacturing facilities that we open, the number of stores that we choose to renovate, and the number and size of any acquisition that we choose make. Our decisions regarding opening, relocating, or renovating stores, and whether to engage in strategic acquisitions, will be based in part on macroeconomic factors and the general state of the U.S. economy, as well as the local economies in the markets in which our stores are located. As of now, we intend to open no fewer than 15 additional stores at an expected aggregate cost of approximately \$26.3 million in the remainder of 2014.

Cash flows

The following table summarizes our cash flow data for the three months ended March 31, 2014 and 2013.

	(in thousands)	
	2014	2013
Net cash provided by operating activities	\$ 15,207	\$ 18,260
Net cash used in investing activities	(11,452)	(11,143)
Net cash provided by (used in) financing activities	(1,229)	5,659

During the three months ended March 31, 2014 and 2013, the Company had net income of \$3.7 million and net loss of \$44.7 million, respectively. Cash from operations during the three months ended March 31, 2014 was \$15.2 million, compared to \$18.3 million during the three months ended March 31, 2013. A decrease in income from operations contributed to the decrease in cash from operations.

Investing activities

Net cash used in investing activities totaled \$11.5 million for the three months ended March 31, 2014, compared to \$11.1 million for the three months ended March 31, 2013. Investing activities for the three months ended March 31, 2014 were primarily for purchases of store fixtures, equipment, building improvements and lease hold improvements for stores opened or remodeled, additions to existing distribution and manufacturing facilities, internally developed software and routine capital purchases of computer hardware and software.

Financing activities

Net cash used in financing activities was \$1.2 million for the three months ended March 31, 2014, compared to cash provided by financing activities of \$5.7 million for the three months ended March 31, 2013. Cash used during the three months ended March 31, 2014 consisted of payments on long term debt and capital lease obligations of \$0.9 million and net payments on the credit facility of \$1.0 million. Principal payments on long-term debt and capital lease obligations over the next 12 months are expected to total approximately \$3.9 million. At March 31, 2014, the Company was in compliance with its debt covenants. The Company intends to pay the principal payments via cash from operations. During the quarter ended March 31, 2013, the Company received \$41.8 million in cash proceeds from the exercise of warrants, and utilized \$30.1 million of that cash to repurchase warrants.

Cash and cash equivalents totaled \$4.3 million at March 31, 2014, versus \$1.8 million at December 31, 2013. The Company has working capital of \$49.3 million at March 31, 2014, compared to working capital of \$51.7 million at December 31, 2013.

Off-balance sheet arrangements

As of March 31, 2014 and December 31, 2013, we did not have any “off-balance sheet arrangements” (as such term is defined in Item 303 of Regulation S-K) that could have a current or future effect on our financial condition, changes in financial condition, net sales or expenses, results of operations, liquidity, capital expenditures or capital resources.

Contractual arrangements

As of March 31, 2014, there were no significant changes to our contractual obligations.

New Accounting Pronouncements

There were no new accounting pronouncements that would have a significant impact on our results of operations, financial condition or liquidity.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to market risks in the ordinary course of our business. These risks include primarily inflation, interest rate risk, and credit concentration risk.

Inflation

Inflationary factors such as increases in the cost of our products and overhead costs may adversely affect our operating results. Although we do not believe that inflation has had a material impact on our financial position or results of operations to date, a high rate of inflation in the future may have an adverse effect on our ability to maintain current levels of gross margin and selling, general, and administrative expenses as a percentage of revenues if the selling prices of our products do not increase with these increased costs.

Interest Rate Risk

We are exposed to interest rate risk through the investment of our cash and cash equivalents and in connection with borrowings under our credit facility. Borrowings under our revolving credit facility bear interest at either a base rate or a LIBOR-based rate, at our option. The LIBOR-based rate ranges from LIBOR plus 1.75% to 2.25%, depending on The Tile Shop's leverage ratio. The base rate will be equal to the greatest of: (a) the Federal funds rate plus 0.50%, (b) the Bank of America "prime rate," and (c) the Eurodollar rate plus 1.00%, in each case plus 0.75% to 1.25% depending on The Tile Shop's leverage ratio. The base rate was 4.25% at March 31, 2014. Based upon balances and interest rates as of March 31, 2014, holding other variables constant, a one percentage point increase in interest rates for the next 12-month period would decrease pre-tax earnings and cash flow of approximately \$1.0 million. Conversely, a one percentage point decrease in interest rates for the next 12-month period would result in an increase to pre-tax earnings and cash flow of approximately \$1.0 million. Changes in interest rates affect the interest income that we earn in connection with these investments, and therefore impact our cash flows and results of operations.

We currently do not engage in any interest rate hedging activity. However, we may do so in the future to mitigate market risk rate. We do not, and do not intend to, engage in the practice of trading derivative securities for profit.

Credit Concentration Risk

Financial instruments, which may subject us to concentration of credit risk, consist principally of cash deposits. We maintain cash balances at financial institutions with strong credit ratings. However, the amounts invested with financial institutions are generally in excess of FDIC insurance limits.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer, Chief Operating Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of March 31, 2014. Based upon that evaluation, the Chief Executive Officer, the Chief Operating Officer and the Chief Financial Officer concluded that such disclosure controls and procedures were effective as of the end of the period covered by this Quarterly Report on Form 10-Q to ensure information required to be disclosed in the reports that the Company files or submits under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission rules and forms, and that it is accumulated and communicated to our management including our CEO, COO and CFO, as appropriate, to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

No changes to our internal control over financial reporting occurred during the quarter ended March 31, 2014 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act). However, we can only give reasonable assurance that our internal controls over financial reporting will prevent or detect material misstatements on a timely basis. Ineffective internal controls over financial reporting could cause investors to lose confidence in our reported financial information and could result in a lower trading price for our securities.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

From time to time, we have been and may become involved in legal proceedings arising in the ordinary course of our business. Although the results of litigation and claims cannot be predicted with certainty, we are not presently involved in any legal proceeding in which the outcome, if determined adversely to us, would be expected to have a material adverse effect on our business, operating results, or financial condition. Regardless of the outcome, litigation can have an adverse impact on us because of defense and settlement costs, diversion of management resources, and other factors.

ITEM 1A. RISK FACTORS

There have been no material changes from the risk factors previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2013.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not Applicable.

ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable.

ITEM 5. OTHER INFORMATION

On March 26, 2014, we amended our credit agreement with Bank of America, N.A. and certain lenders to adjust the calculation of certain financial covenants. The foregoing summary is not complete and is qualified in its entirety by reference to the full text of the amendment, a copy of which is set forth as Exhibit 10.1 to this Quarterly Report on Form 10-Q and is incorporated by reference herein.

ITEM 6. EXHIBITS

Exhibits

- 3.1⁽¹⁾ Certificate of Incorporation of Tile Shop Holdings, Inc.
- 3.2⁽²⁾ By-Laws of Tile Shop Holdings, Inc.
- 10.1* Amendment No. 3 to Credit Agreement, dated as of March 26, 2014, by and among Tile Shop Holdings, Inc., The Tile Shop, LLC, certain subsidiaries of The Tile Shop, LLC and Bank of America, N.A., as Administrative Agent, Swing Line Lender, and L/C Issuer.
- 31.1* Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes Oxley Act of 2002.
- 31.2* Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes Oxley Act of 2002.
- 32.1** Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes Oxley Act of 2002.
- 32.2** Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes Oxley Act of 2002.
- 101.INS XBRL Instance Document.
- 101.SCH XBRL Taxonomy Extension Schema Document.
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase Document.
- 101.DEF XBRL Taxonomy Extension Definition Linkbase Document.
- 101.LAB XBRL Taxonomy Extension Label Linkbase Document.
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase Document.
- (1) Filed as Exhibit 3.1 to the Registrant's Registration Statement on Form S-4 filed with the Securities and Exchange Commission on July 2, 2012, and incorporated herein by reference.
- (2) Filed as Exhibit 3.2 to the Registrant's Registration Statement on Form S-4 filed with the Securities and Exchange Commission on July 2, 2012, and incorporated herein by reference.
- * Filed herewith.
- ** Furnished herewith.
- + In accordance with Rule 406T of Regulation S-T, these XBRL (eXtensible Business Reporting Language) documents are furnished and not filed or a part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, or Section 18 the Securities Exchange Act of 1934, as amended, and otherwise are not subject to liability under these sections

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

TILE SHOP HOLDINGS, INC.

Dated: May 9, 2014

By: /s/ Robert A. Rucker
Robert A. Rucker
Chief Executive Officer

Dated: May 9, 2014

By: /s/ Timothy C. Clayton
Timothy C. Clayton
Chief Financial Officer

TILE SHOP HOLDINGS, INC.
EXHIBIT INDEX

Exhibit No.	Description
3.1(1)	Certificate of Incorporation of Tile Shop Holdings, Inc.
3.2(2)	By-Laws of Tile Shop Holdings, Inc.
10.1*	Amendment No. 4 to Credit Agreement, dated as of March 26, 2014, by and among Tile Shop Holdings, Inc., The Tile Shop, LLC, certain subsidiaries of The Tile Shop, LLC and Bank of America, N.A., as Administrative Agent, Swing Line Lender, and L/C Issuer.
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*	Filed herewith.
**	Furnished herewith.

+ In accordance with Rule 406T of Regulation S-T, these XBRL (eXtensible Business Reporting Language) documents are furnished and not filed or a part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, or Section 18 the Securities Exchange Act of 1934, as amended, and otherwise are not subject to liability under these sections

AMENDMENT NO. 3 TO CREDIT AGREEMENT

This Amendment No. 3 to Credit Agreement (this "**Third Amendment**") dated as of March 26, 2014, is made by and among **TILE SHOP HOLDINGS, INC.**, a Delaware corporation ("**Holdings**"), **THE TILE SHOP, LLC**, a Delaware limited liability company (the "**Company**"), **TILE SHOP LENDING, INC.**, a Delaware corporation ("**Tile Shop Lending**"), certain Subsidiaries of the Company party hereto as borrowers (each such Subsidiary and Tile Shop Lending, a "**Designated Borrower**" and, together with the Company, the "**Borrowers**" and, each a "**Borrower**"), certain Subsidiaries of the Company party hereto as guarantors (each such Subsidiary, a "**Subsidiary Guarantor**" and, together with Holdings, the "**Guarantors**" and each a "**Guarantor**"), each lender party hereto (collectively, the "**Lenders**" and individually, a "**Lender**"), and **BANK OF AMERICA, N.A.**, as Administrative Agent (the "**Administrative Agent**"), a Swing Line Lender and an L/C Issuer.

WITNESSETH:

WHEREAS, certain of the Borrowers, Holdings, the Administrative Agent and the Lenders have entered into that certain Credit Agreement dated as of October 3, 2012 (as amended by that certain Amendment No. 1 to Credit Agreement dated as of April 30, 2013, Amendment No. 2 to Credit Agreement dated as of July 8, 2013, and as further amended, modified, supplemented, restated, or amended and restated to, but not including, the date hereof, the "**Credit Agreement**"; the capitalized terms used in this Third Amendment not otherwise defined herein shall have the respective meanings given thereto in the Credit Agreement), pursuant to which the Lenders have made available to certain of the Borrowers a term loan facility and a revolving credit facility; and

WHEREAS, the Borrowers have requested that the Administrative Agent and the Lenders agree to amend certain terms of the Credit Agreement, which the Administrative Agent and the Lenders are willing to do on the terms and conditions contained in this Third Amendment.

NOW, THEREFORE, in consideration of the premises and further valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

1. Amendments to Credit Agreement. Subject to the terms and conditions set forth herein, the Credit Agreement is hereby amended as follows:

(a) The definition of "Capital Expenditures" in Section 1.01 of the Credit Agreement is hereby amended to read in its entirety as follows:

"Capital Expenditures" means, with respect to any Person for any period, any expenditure in respect of the purchase or other acquisition of any fixed or capital asset. For purposes of this definition, the purchase price of equipment that is purchased simultaneously with the trade-in of existing equipment or with insurance proceeds shall be included in Capital Expenditures only to the extent of the gross amount by which such purchase price exceeds the credit granted by the seller of such equipment for the equipment being traded in at such time or the amount of such insurance proceeds, as the case may be."

(b) The following definition of “Third Amendment Effective Date” is hereby added to Section 1.01 of the Credit Agreement to read as follows:

““Third Amendment Effective Date” means, March 26, 2014.”

(c) Section 7.11(b) of the Credit Agreement is hereby amended to read in its entirety as follows:

“(b) Consolidated Total Rent Adjusted Leverage Ratio. Permit the Consolidated Total Rent Adjusted Leverage Ratio at any time during any period of four fiscal quarters of Holdings set forth below to be greater than the ratio set forth below opposite such period:

<u>Four Fiscal Quarters Ending</u>	<u>Maximum Consolidated Total Rent Adjusted Leverage Ratio</u>
Third Amendment Effective Date through September 30, 2014	4.00 to 1.00
December 31, 2014	3.75 to 1.00
March 31, 2015 and each fiscal quarter thereafter	3.50 to 1.00

(d) Section 7.12 of the Credit Agreement is hereby amended to read in its entirety as follows:

“**7.12 Capital Expenditures**. For the fiscal year ending December 31, 2014, make or become legally obligated to make Capital Expenditures in excess of \$42,500,000 in the aggregate for Holdings and its Subsidiaries during such fiscal year.”

2. Effectiveness; Conditions Precedent. The parties hereto agree that upon the satisfaction of each of the following conditions precedent all amendments contained herein below shall be effective (the “**Third Amendment Effective Date**”):

(a) the Administrative Agent shall have received counterparts of this Third Amendment, duly executed by each Borrower, each Guarantor, the Administrative Agent and each of the Lenders, which counterparts may be delivered by telefacsimile or other electronic means (including .pdf); and

(b) both (i) an amendment fee shall have been received by the Administrative Agent for each Lender executing this Third Amendment by 5:00 p.m. (New York time) on March 26, 2014 for the account of such Lender, paid to the Administrative Agent, equal to 0.075% (7.5 bps) multiplied by (A) in the case of the Revolving Credit Lenders, each such Revolving Credit Lender's Revolving Credit Commitment as of the Third Amendment Effective Date and (B) in the case of the Term Lenders, each such Term Lender's Outstanding Amount of Term Loans as of the Third Amendment Effective Date; and (ii) all other reasonable fees and expenses incurred or payable in connection with the execution and delivery of this Third Amendment (including the reasonable fees and expenses of counsel to the Administrative Agent to the extent due and payable under Section 10.04(a) of the Credit Agreement) shall have been paid in full.

3. Representations and Warranties. In order to induce the Administrative Agent and the Lenders to enter into this Third Amendment, each of Holdings and each Borrower represents and warrants to the Administrative Agent and the Lenders as follows:

(a) The representations and warranties made by each of Holdings and each Borrower in Article V of the Credit Agreement and in each of the other Loan Documents to which it is a party are true and correct in all material respects on and as of the date hereof, except to the extent that such representations and warranties expressly relate to an earlier date;

(b) This Third Amendment has been duly authorized, executed and delivered by the Borrowers and the Guarantors party hereto and constitutes a legal, valid and binding obligation of such parties, subject to applicable Debtor Relief Laws and subject to general principles of equity, regardless of whether considered in a proceeding in equity or at law;

(c) The Persons appearing as Guarantors on the signature pages to this Third Amendment constitute all Persons who are required to be Guarantors pursuant to the terms of the Credit Agreement and the other Loan Documents (after giving effect to this Third Amendment), and each of such Persons has become and remains a party to a Guaranty as a Guarantor; and

(d) As of the Third Amendment Effective Date, no Default or Event of Default has occurred and is continuing.

4. Entire Agreement. This Third Amendment, together with all the Loan Documents (collectively, the "**Relevant Documents**"), sets forth the entire understanding and agreement of the parties hereto in relation to the subject matter hereof and supersedes any prior negotiations and agreements among the parties relating to such subject matter. No promise, condition, representation or warranty, express or implied, not set forth in the Relevant Documents shall bind any party hereto, and no such party has relied on any such promise, condition, representation or warranty. Each of the parties hereto acknowledges that, except as otherwise expressly stated in the Relevant Documents, no representations, warranties or commitments, express or implied, have been made by any party to the other in relation to the subject matter hereof or thereof. None of the terms or conditions of this Third Amendment may be changed, modified, waived or canceled orally or otherwise, except in writing and in accordance with Section 10.01 of the Credit Agreement.

5. Full Force and Effect of Agreement. Except as hereby specifically amended, modified or supplemented, the Credit Agreement and all other Loan Documents are hereby confirmed and ratified in all respects and shall be and remain in full force and effect according to their respective terms.

6. Counterparts. This Third Amendment may be executed in any number of counterparts, each of which shall be deemed an original as against any party whose signature appears thereon, and all of which shall together constitute one and the same instrument. Delivery of an executed counterpart of a signature page of this Third Amendment by telecopy or other electronic means (including .pdf) shall be effective as delivery of a manually executed counterpart of this Third Amendment.

7. Governing Law. This Third Amendment shall in all respects be governed by, and construed in accordance with, the laws of the State of New York applicable to contracts executed and to be performed entirely within such State, and shall be further subject to the provisions of Sections 10.14 and 10.15 of the Credit Agreement.

8. Enforceability. Should any one or more of the provisions of this Third Amendment be determined to be illegal or unenforceable as to one or more of the parties hereto, all other provisions nevertheless shall remain effective and binding on the parties hereto.

9. References. From and after the Third Amendment Effective Date, all references in the Credit Agreement and any of the other Loan Documents to the “Credit Agreement” shall be deemed to be references to the Credit Agreement, as amended or modified hereby.

10. Successors and Assigns. This Third Amendment shall be binding upon and inure to the benefit of the Borrowers, the Administrative Agent and each of the Guarantors and Lenders, and their respective successors, legal representatives, and assignees to the extent such assignees are permitted assignees as provided in Section 10.06 of the Credit Agreement.

[Signature pages follow.]

IN WITNESS WHEREOF, the parties hereto have caused this instrument to be made, executed and delivered by their duly authorized officers as of the day and year first above written.

THE TILE SHOP, LLC

By: /s/ Timothy C. Clayton

Name: Timothy C. Clayton

Title: Senior Vice President & CFO

Amendment No. 3

Signature Page

TILE SHOP LENDING, INC.

By: /s/ Timothy C. Clayton

Name: Timothy C. Clayton

Title: President & CFO

Amendment No. 3

Signature Page

GUARANTORS:

TILE SHOP HOLDINGS, INC.

By: /s/ Timothy C. Clayton

Name: Timothy C. Clayton

Title: Senior Vice President & CFO

THE TILE SHOP OF MICHIGAN, LLC

By: /s/ Timothy C. Clayton

Name: Timothy C. Clayton

Title: Senior Vice President & CFO

Amendment No. 3
Signature Page

BANK OF AMERICA, N.A., as Administrative Agent

By: /s/ Roberto Salazar

Name: Roberto Salazar

Title: Vice President

Amendment No. 3

Signature Page

BANK OF AMERICA, N.A., as a Lender, L/C Issuer and Swing Line Lender

By: /s/ A. Quinn Richardson

Name: A. Quinn Richardson

Title: Senior Vice President

Amendment No. 3

Signature Page

THE HUNTINGTON NATIONAL BANK, as a Lender

By: /s/ Marc D. Adams

Name: Marc D. Adams

Title: Vice President

Amendment No. 3
Signature Page

CERTIFICATION UNDER SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Robert A. Rucker, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Tile Shop Holdings, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: May 9, 2014

By: /s/ Robert A. Rucker
Robert A. Rucker
Chief Executive Officer

CERTIFICATION UNDER SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Timothy C. Clayton, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Tile Shop Holdings, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: May 9, 2014

By: /s/ Timothy C. Clayton
Timothy C. Clayton
Chief Financial Officer

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED
PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

Pursuant to 18 U.S.C. §1350 (as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002), I, Robert A. Rucker, the Chief Executive Officer of Tile Shop Holdings, Inc. (the "Company"), hereby certify that the Quarterly Report on Form 10-Q of the Company for the quarter ended March 31, 2014 ("the Report") fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the SEC or its staff upon request.

Dated: May 9, 2014

By: /s/ Robert A. Rucker
Robert A. Rucker
Chief Executive Officer

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED
PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

Pursuant to 18 U.S.C. §1350 (as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002), I, Timothy C. Clayton, the Chief Financial Officer of Tile Shop Holdings, Inc. (the "Company"), hereby certify that the Quarterly Report on Form 10-Q of the Company for the quarter ended March 31, 2014 (the "Report") fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the SEC or its staff upon request.

Dated: May 9, 2014

By: /s/ Timothy C. Clayton
Timothy C. Clayton
Chief Financial Officer